

COMMISSION ON TAX POLICY IN THE NEW ECONOMY

TAX POLICY REFORMS

William J. Rosendahl, Presentation at the Little Hoover Commission, March 25, 2004

Sales Tax

(1) The Commission held hearings on whether California should join the **Streamlined Sales Tax Project (SSTP)** as a voting member.

- Governor Davis signed SB 157 (Bowen) in October 2003, making California a voting member of the SSTP.¹

(2) **Recommendation (unanimous):** Efforts should be made by the Board of Equalization to improve collection of the use tax that is currently California law.

- Governor Davis signed SB 1009 (Alpert) in September 2003, adding a line to the personal income tax form for the reporting of use tax. This bill also prohibits the state from contracting with a vendor, contractor, or an affiliate of a vendor or contractor that does not possess a seller's permit or a certificate of registration. This bill takes effect on New Year's Day, 2004.
- AB 694 (Levine) would expand use tax on boats and airplanes bought out of state. This bill is currently inactive.

(3) **Recommendation:** Broaden the sales tax base to include selected services, while lowering the state rate to retain revenue neutrality.

- No legislative action

(4) **Recommendation for Further Study (unanimous):** Eliminate selected sales and use tax exemptions or exclusions.

- AB 990 (Ridley-Thomas) Requires the Legislative Analyst to annually prepare a tax expenditure report and make recommendations.
- AB 923 (Firebaugh) Repeals sales tax exemption on tractors, farm diesel, race horses and timber equipment. These exemptions are summarized at:
<http://www.boe.ca.gov/sutax/sutexempt.htm>

¹ To represent California and vote at SSTP meetings, SB 157 established a Board of Governance consisting of two Members of the Senate chosen by the Senate Committee on Rules, two Members of the Assembly chosen by the Speaker of the Assembly, one member of the State Board of Equalization, one member of the Franchise Tax Board, and one member of the Governor's Department of Finance.

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Property Tax

(5) Recommendation: Property/Sales Tax Swap: Change the mix of local general-purpose revenue by decreasing the amount of sales tax revenue and replacing it with property tax revenue. The objective of this proposal is to decrease local reliance on the sales tax and increase reliance on the property tax.

- ACA 17 (Daucher) Shift between local sales and property tax.
- AB 421 (Steinberg) Amendment to budget triple-flip; repeals the property tax back-fill.
- SB 1212 (Ducheny) Eliminates VLF backfill, gas tax and hoe reimbursement payments to locals; Replaced with property tax.
- AB 1221 (Campbell/Steinberg) Property/sales tax swap – Inactive bill.

California Home Rule Amendment

Initiative Type: Constitutional Amendment.

Signatures are being collected for the November 2004 election.

Signature collection deadline: April 30, 2004.

Signatures needed: 598,105

“This amendment will give local government a reliable and growing source of revenue.”

It will:

1. Give local governments an increased share of local property taxes. Local governments will exchange ½ cent of their Bradley-Burns sales tax and their VLF revenues for increased shares of property taxes. When property tax revenues increase, local governments share in the increased revenues.
2. Protect local government finances. Local government revenues will be constitutionally guaranteed through an expansion of the definition of local mandates and constitutional provisions prohibiting the reassignment or state taking of any locally-raised funds.

<http://www.calhomerule.com/>

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Property Tax (continued)

(6) Recommendation for Further Study: Periodically reassess non-residential property to market value without changing existing rates and in the context of improving the business climate in California.

- ACA 16 (Hancock) Repeals Proposition 13 Assessment Standard for non-residential, non-agricultural property
- SB 17 (Escutia) Stricter reporting requirements for publicly held corporations; higher penalties. This bill is currently inactive.

Improving Classroom Education Act (ICEA)

(California Teacher's Association, Robert Reiner, Split Roll Initiative for the November 2004 ballot)

This Act will provide substantial new funding to California's K-12 public school classrooms to reduce class size, buy textbooks and materials, raise teacher salaries and pay for teacher training. It also provides funding for universal access to quality preschool for all California children the year before they start kindergarten. In addition, the initiative provides personal property tax relief to all California businesses.

Initiative funding: The ICEA raises more than \$4.5 billion for public education by raising the tax on commercial property from 1% to 1.55%. It does not raise property taxes for California homeowners.

- Owner-occupied residential property, agricultural property, open space and historically significant property, timberland and government property are excluded.
- Residential rental property assessed at less than \$700,000 is also exempted. Property taxes on other residential property are raised on a sliding scale from \$700,000 (1.1%) to \$1,000,000 and above (1.55%).
- The initiative protects the state against any loss of income due to the raising of property taxes.
- The initiative sets aside 10% of the funds raised to provide a personal property tax exemption for businesses, principally for small business owners.

<http://www.caltax.org/SplitRoll1-9-04.pdf>

http://www.cta.org/CaliforniaEducator/v8i3/Stand_1.htm

<http://www.cta.org/Features/ICEA/ICEA.htm>

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Local Taxes

(7) Recommendation: Provide a constitutional minimum allocation of property taxes to local government.

Local Taxpayers and Public Safety Protection Act

The Local Taxpayers and Public Safety Protection Act is an initiative sponsored by the League of California Cities, the California State Association of Counties and the California Special District Association. Planned for the November 2004 statewide ballot, the measure is intended to increase local control over local tax dollars, so that funding for critical local services is more dependable and predictable.

The initiative would require a majority vote of the people before the state government would be allowed to take and use local government funds. It also strengthens existing law that says when the state mandates a program, service or added cost to local governments, the state must reimburse the local governments in a timely manner for the cost of providing that program or service.

<http://www.cacities.org/>

California Home Rule Amendment

See description under the Property/Sales Tax Swap

<http://www.calhomerule.com/>

(8) Recommendation: Reduce the vote threshold now required for approval of local special tax measures from two-thirds to 55 percent.

- SCA 11 (Alarcon) 55% vote for special taxes and tax-supported bonds when proceeds used for infrastructure.

Inactive bills:

- ACA 9 (Levine) Majority vote for local special taxes
- ACA 11 (Levine) Majority vote for local infrastructure bonds, over ride of Prop 13 1% tax rate.
- ACA 14 (Steinberg) Local governments could impose majority vote transportation and use taxes for infrastructure.

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Other Tax Policy Options

(9) Recommendation (unanimous): State Tax Court: California should establish a state administrative body to operate like the U.S. tax court. This body would resolve all tax disputes, including personal income tax, corporate income tax, sales and use tax, property taxes, payroll taxes, and excise taxes as outlined in Professor Simmons' September 23, 2003 letter to the Commission.

- AB 2472 (Wolk) Establishes a state tax court.

(10) Recommendation for Further Study: Flat-Rate Tax Proposal - Eliminate all current taxes in California except for “sin taxes,” such as cigarette and alcohol taxes, and establish two new taxes, a six-percent flat-rate personal income tax and a six-percent flat-rate business value-added-tax.

- No Action

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Recommended Reforms of the State Budget Process

(11) Recommendation (unanimous): Amend the California Constitution to do the following:

- 1) **Revise the current spending limit** - In order to make the spending limit more transparent, revise it to limit spending based on population and economic growth.
- 2) **Reserve requirement** - In order to reduce the fiscal shock of an economic downturn, require the maintenance of a reserve.
- 3) **Rebalancing an unbalanced budget** - Establish a system for rebalancing the state budget when it becomes unbalanced.
- 4) **Multi-year budget planning requirement** - Initiate a fiscal planning requirement that will require the state budget process to plan longer than 12 months.
- 5) Implement changes that would foster a “**culture of accountability**” in the budget process.²

Proposition 58, which was passed by the voters in March 2004, addressed some of these recommendations. Proposition 58 will:

- Establish a process for consideration of midyear budget adjustments. This will allow the Governor to proclaim a fiscal emergency in specified circumstances and submit proposed legislation to address the fiscal emergency. Requires the Legislature to stop other action and act on legislation proposed to address the emergency.
- Balanced budget requirement – Require enactment of a balanced budget where General Fund expenditures do not exceed estimated General Fund Revenues.
- Establish a budget reserve.
- Provide that the California Economic Recovery Bond Act is for a single object or work.
- Prohibit any future deficit bonds.

² As per the recommendations from the Bay Area Council and the Speaker’s Commission on State and Local Government Financing.